MORTGAGE BULLETIN

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BATTLE DRESS ON THE MORTGAGE FRONT

WHEN cold war becomes hot everything looks different. Up until June 25 Korea was little more than a name to most United States citizens, and the "38th Parallel" seemed like a relic of the Lewis and Clark Expedition. But now every other problem, domestic or international, fades into insignificance before the fierce conflict which carries with it the fearsome threat of world war. Korea has in fact torn the veil of illusion from the stern face of reality. It restores a sense of proportion in human affairs by putting things in their proper order. We recognize the chapter for what it is: a preliminary bout that will alert us to be prepared for any and all eventualities. The struggle in Korea may well last a long time, and it's a deadly serious struggle -- to those who must fight it, and to us who must support it.

The impact of war upon a record business boom is bringing expected results. Inflationary forces are intensifying and anticipatory buying has been sweeping the country. Many manufacturers and builders fearing higher prices and shortages are buying key materials far ahead of current requirements in an effort to build inventory before the passage of the pending Defense Production Act, with its provisions for priorities and allocations, limitation on the use of materials for nonessential purposes, inventory controls and credit restrictions. Likewise, consumers are bent on forestalling another section of the same Act -- the section which would tighten credit terms for the purchase of automobiles, houses and other durable goods.

The business boom of recent months has been predominantly a boom in durable goods centering largely in housing. It would be neither fair nor accurate to say that the expansion of the housing industry has been the result solely of credit expansion. On the other hand, construction is a field in which expansion thrives on low-cost money and easy credit terms. The outlays for new dwelling units from January through July of this year were up 60 per cent, totaling more than $5.8 billion. In July expenditures on new dwellings rose to $1,110 million compared with $659 million in the same month of 1949. New permanent nonfarm dwelling units started in July were 144,000, which brought housing "starts" from the first of the year to almost 839,000. For the twelve months from August 1949 through July 1950 the figures show that 1,318,300 nonfarm units were started, which is an all-time record for the building industry.

A corollary of this amazing building activity is an outstanding nonfarm mortgage debt in excess of $40 billion, practically double what it was at the end of 1945. New nonfarm mortgages, $20,000 or less, recorded from January through July averaged approximately $1,250 million per month. A remarkable feature in the

situation is the subsidence of expressions of uneasiness, which were so frequently heard during 1948, over the alarming increase in home mortgage debt and in the liabilities of the Federal government which insures so many of these mortgages. It is clearly apparent that this huge debt attracts less attention the more people become habituated to it.

Under a war economy the expansion of mortgage debt which has accompanied the forced-draft housing boom, and with which it is inseparably connected, necessitated a complete reversal of policy by the Administration for home financing. As a necessary step in the public interest and to conserve materials needed for the public defense, President Truman on July 18 acted by means of directives to restrict immediately the spending of the Housing and Home Finance Agency, the Veterans Administration, and the Reconstruction Finance Corporation in the housing area. Ostensibly, Mr. Truman's directives are rather vigorous curbs on mortgage financing, but in actuality they are only homeopathic doses where allopathic treatment for the patient was indicated. The new set-up has been gracefully accepted by most institutional lenders and builders as many of them had become uneasy over the increasing number of "shoestring" purchases.

Conservative bankers with whom I have discussed the question hold the opinion that Washington is highly conscious of the leading role which expanding construction activities have played in keeping business humming during the postwar years. They have a strong conviction that the government is far from anxious to throw a monkey-wrench into the machinery while it is operating in high gear. As sustaining evidence of their conviction Tighe E. Woods, Housing Expediter, speaking before the Pennsylvania Institute, School of Trades, in Philadelphia on August 10, was reported as saying that construction of new houses in the United States has not halted. He further insisted that there was no law on the books or under consideration by Congress "that would call for a curtailment of housing construction." This statement lends added significance to the accelerated pace at which builders in the Greater New York City area have been acquiring land during the past few weeks. It is our guess that the present rate of housing starts has been given the green light for another sixty or ninety days and then may be cut back by further restrictions on mortgage credit rather than by priorities and allocations. Housing is still the "court favorite" at Washington.

At the moment the mortgage business is good. Some of the large city savings and loan associations have been receiving more applications than they could comfortably process. FHA has experienced a falling off in applications for loans on new homes, while the applications for refinancing loans on existing properties have been increasing. This was indicated by the figures at the end of 1949 and confirmed currently by an FHA official. Business is excellent with the Veterans Administration and loans granted have been running about double what they were a year ago. The 60 per cent guaranty was icing added to the cake which made it more toothsome. The 5 per cent down payment may slow VA activity slightly, but as VA mortgages are mostly on modest homes the 5 per cent cash required should not prove to be very onerous. RFC's little helper in the mortgage field, Fannie May, was directed by the President "that further mortgage purchases are to be held to the irreducible minimum." While it is true that FNMA is limiting itself to over-the-counter transactions, we have heard that the interpretation of "irreducible minimum" is turning out to be quite elastic in application. In the New York office of Fannie May mort-

gage sales are stepping right along with further large sales in prospect. About September 7 the FNMA program shifts to the Housing and Home Finance Agency, and there are strong hints that Administrator Raymond Foley favors selling Fannie May's mortgages at par.

Congressman Dwight L. Rogers of Florida has proposed a bill to aid those in the military service which mortgagees in all probability would consider a timely piece of legislation. The Rogers bill would provide funds for advancing payments of interest and principal on mortgages not in excess of $20,000 and to make rent payments up to $100 per month. In substance these advances would be non-interest-bearing loans from the government to the serviceman. Such advances could be repaid over a period four times the length of the period during which advances are made. Volunteers would be covered by these provisions as well as those called to active duty, and the provisions would apply to all mortgages whether guaranteed by the government or not. Amid plaudits, or regrets, depending on one's viewpoint, Rep. Rogers' proposal has been referred to the Committee on Veterans' Affairs.

Under the Soldiers' and Sailors' Relief Act of 1940, which is still in force, housing investments of those in military service generally will not be imperiled. One of the provisions of the Act is the protection of military personnel against attachment of property, or garnishment for debts in the hands of another. Another provision prevents eviction from premises renting for not in excess of $80 per month and used principally as a dwelling for the serviceman's wife, children or other dependents. The law further affords protection against repossession for nonpayment of installments on purchased property and against collection of property taxes falling due during military service. The provisions of the Act cover all branches of the service and Public Health Service officers detailed to duty with the armed services. It also covers not alone those on active duty but the individuals taking training or education under the supervision of the government before induction into the military service. Sections of the law which were annulled by the proclamation of the termination of hostilities in 1947 were reinstated by the Draft Act of 1950, and there seems small doubt that the regulations will be extended further as the need comes up.

It begins to appear that married men expecting to volunteer or to be called into service are becoming cognizant of their rights under the Soldiers' and Sailors' Act. We have it on unimpeachable authority that some of them have been hurrying to buy homes and assume mortgage obligations prior to induction. This brings up a problem of no small moment for the mortgage bankers and other mortgage lenders. With the protection provided under the Act for those actively in service, is a bank, for example, justified in rejecting an application for mortgage financing from a person expecting to enter service? If it happened to be a case where a commitment had previously been made, it would seem that the bank is obligated to go through with the original commitment. Under any other circumstances we believe it would be within the bank's discretion as to whether or not the loan application would be accepted. Some bankers think that on a loan made to a man expecting to be inducted into service the cushion between the amount of the loan and the market value of the property, plus the price appreciation they look for as a result of heavy war expenditures, would offset the increase in the mortgagor's indebtedness while he is in the armed service. At the expiration of his "hitch" in the service the loan could be

extended. We have been advised that this problem, with its several angles, is being studied.

In our Mortgage Bulletin of last March we commented briefly on the so-called "open-end" mortgage. This method of mortgage financing is generating increasing interest as it provides a low-cost outlet for additional funds. Basically, the open-end mortgage is a device whereby as the original loan is reduced by amortized payments, further advances can be made to the mortgagor by adding such advances to the mortgage balance with the original amount of the loan as the maximum. The appraised value of the property, at the time of each advance, must be adequate to secure the total indebtedness.

Recently a sub-committee of the Savings Banks Association of the State of New York made a study of the open-end mortgage and came up with so favorable a report on its suitability for both lender and borrower that preparations are now under way for its adoption by the New York State savings banks generally. This move will probably influence many other savings banks to embrace this type of financing. The open-end, or escalator, clause in a mortgage contract has been demanding attention as a means of financing real estate repairs and improvements. By saving additional mortgage tax, expenses of title examination and other costs, the open-end feature of a mortgage is a powerful incentive for the mortgagor to borrow additional funds from the original lender rather than go elsewhere. Further borrowing from other sources, after the creation of the original loan, often results in overextension of credit to mortgagors and in some cases causes delinquencies and foreclosures. It has come to our attention that several manufacturers of household appliances are highly in favor of the open-end feature as it provides a source for funds for the purchases of their products. It seems more than likely that the open-end mortgage will become an increasingly important factor in home financing.

Shortly after the market for government securities closed on August 19, two extraordinary announcements were made from Washington. The Federal Reserve Board raised the discount rate of the Federal Reserve Bank of New York from $1\frac{1}{2}$ per cent to 1-3/4 per cent to tighten bank credit and make money more costly. At the same time Secretary John Snyder indicated that the Treasury wants no increase in loan rates by bluntly announcing that the impending refunding by the Treasury of $13, 570, 000, 000 of bonds and certificates of indebtedness would be by two offerings of 13-month notes bearing the same 1-1/4 per cent as on recent issues. Secretary Snyder simultaneously invited savings banks, insurance companies and other institutional investors to increase ten-fold their permissible holdings of F and G savings bonds. If the investing institutions avail themselves of this privilege it would syphon off a vast amount of funds, a substantial part of which might otherwise go into financing housing. Of course, these measures were promulgated to reduce the lending potential of banks and other institutional investors collecting the savings of the public. One cannot escape the conclusion that the Treasury wants cheap money, the Federal Reserve does not.

From my position as an observer on the mortgage front, trying to figure out what lies ahead is like attempting to peer through a glass of roiled water. However, glancing backward over the happenings that have shaken the stability of our economy during the past few months, would seem to warrant a few conclusions.

SPECIMEN OF AN OPEN-END RIDER TO BE ATTACHED TO A MORTGAGE CONTRACT

To Elm Street Federal Savings and Loan Association
2514 Elm Street, St. Louis 18, Missouri

To be attached to Mortgage recorded in Book 36, Page 964 (Register or clerk) County of Franklin, Missouri

In addition to the agreements, covenants and conditions contained in the mortgage to which this rider is attached and of which it forms a part, it is further agreed by and between the parties hereto:

Upon request of the mortgagor, the mortgagee may hereafter, at its option, at any time before full payment of this mortgage, make further advances to the mortgagor, and any such further advance, with interest, shall be secured by this mortgage and shall be evidenced by an additional bond or agreement then to be given by the mortgagor; provided, however, that the amount of principal secured by this mortgage and remaining unpaid, shall not at the time of and including any such advance exceed the original principal sum secured hereby.

The mortgagor does covenant and agree to and with the mortgagee to repay all such further advances made as aforesaid with interest; that such further advances and each bond or agreement evidencing the same shall be secured by this mortgage; and that all of the covenants and agreements in this mortgage contained shall apply to such further advances as well as to the original principal sum herein recited.

The word "mortgagee" as used in this rider shall be construed to mean the owner and holder of the security instrument to which this rider is attached, or any assignee or transferee thereof. The word "mortgagor" as used in this rider shall be construed to mean the maker or makers of said security instrument, and also the vendees, devisees, successors, heirs and assigns of such mortgagor; the word "mortgage" as used in this rider shall be construed to mean the security instrument to which this rider is attached.

In consideration of the Elm Street Federal Savings and Loan Association making a further advance of $500.00 we agree to the above and consent to the same being attached to the original mortgage.

L. S. ______________________________

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In Presence of

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The over-all picture, as the New York Times reported on August 23, is one in which total defense costs, military and economic, will amount to approximately $35 billion in 1951, and may reach $50 billion in 1952 and 1953. Moreover, this huge spending program finds us in the price inflation phase of a major domestic boom. Nowhere can the fever chart of America be better read than in the soaring construction figures. The sound of the hammer and saw was not a decibel lower in mid-August than it was during the record month of July. Builders evidently believe that the productive miracle of America can supply military needs without in any important way reducing the flow of building materials. The building boom will roll on at high level as long as builders can arrange construction loans and the buyers finance home purchases on a "shoestring." There is nothing in this picture to justify a stampede for the adoption of harsh wartime controls, but it does underscore, it seems to us, the significance of one thing -- a decisive tightening of real estate credit.

The United States is fighting two major actions - a military conflict in Korea, and a fight against inflationary pressures at home. We will win the struggle in Korea but we may lose the fight against inflation.

E. G. Johnson

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